

DEPARTMENT OF STATE REVENUE

Commissioner's Directive #14
October 2013
(Replaces Directive #14 Issued August 2011)
Effective Dates: January 1, 2013, and July 1, 2013

SUBJECT: Financial Institutions Tax

REFERENCE: [IC 6-5.5](#)

DISCLAIMER: Commissioner's directives are intended to provide nontechnical assistance to the general public. Every attempt is made to provide information that is consistent with the appropriate statutes, rules, and court decisions. Any information that is not consistent with the law, regulations, or court decisions is not binding on either the department or the taxpayer. Therefore, the information provided herein should serve only as a foundation for further investigation and study of the current law and procedures related to the subject matter covered herein.

SUMMARY OF CHANGES

This version of the directive has been changed to reflect provisions of HEA 1001-2013, which eliminate several addbacks in determining adjusted gross income, and HEA 1018-2013, which reduces the financial institutions tax rate from 8.5 percent to 6.5 percent over the next four fiscal years.

INTRODUCTION

The purpose of this directive is to present an overview of the Indiana financial institutions tax (FIT). This overview is intended to highlight the major areas of the law and promote a general understanding of its basic principles.

Any taxpayer taxable under [IC 6-5.5](#) is exempt from Indiana's adjusted gross income tax.

The law extends Indiana's tax jurisdiction to both resident and nonresident financial institutions and to all corporate entities that transact the "business of a financial institution" in Indiana regardless of where such entity is domiciled.

[IC 6-5.5](#) adopts an economic presence method for determining the jurisdictional basis for taxing nonresidents who conduct the business of a financial institution in Indiana.

DEFINITIONS

"Business of a financial institution" means the activities of a traditional financial institution, or any corporation that derives 80 percent or more of its income from making, acquiring, servicing, or selling loans or extending credit.

If a transaction is treated as a lease for federal income tax purposes, the leasing transaction is not the economic equivalent of extending credit for purposes of the 80 percent test. However, for purposes of the 80 percent test, extending credit not only includes credit card operations, but also includes debit card, charge card, and similar businesses.

"Taxpayer" means regulated financial institutions, their holding companies, and the subsidiaries of either, as well as any other corporation (including entities taxed as a corporation under the Internal Revenue Code) organized under the laws of the United States, Indiana, another taxing jurisdiction, or a foreign government that is carrying on the business of a financial institution in Indiana.

Taxpayers are differentiated on the basis of their resident or nonresident status. A resident taxpayer is a taxpayer that is commercially domiciled in Indiana and transacts the business of a financial institution in Indiana.

A nonresident taxpayer is a taxpayer that is not commercially domiciled in Indiana but transacts the business of a financial institution in Indiana. [IC 6-5.5-3](#) establishes the rules for determining when the activities of nonresident corporations constitute transacting business in Indiana. A taxpayer is transacting business in Indiana for the purposes of the FIT when it satisfies any of the following eight tests:

- (1) Maintains an office in Indiana;
- (2) Has an employee, a representative, or an independent contractor conducting business in Indiana;
- (3) Regularly sells products or services of any kind or nature to customers in Indiana that receive the product or service in Indiana;

- (4) Regularly solicits business from potential customers in Indiana;
- (5) Regularly performs services outside Indiana that are consumed within Indiana;
- (6) Regularly engages in transactions with customers in Indiana that involve intangible property, including loans, but not property described in [IC 6-5.5-3-8](#)(5), and result in receipts flowing to the taxpayer from within Indiana;
- (7) Owns or leases intangible personal or real property located in Indiana; or
- (8) Regularly solicits and receives deposits from customers in Indiana.

Only a portion of a nonresident taxpayer's income is subject to the FIT. The statute employs a single-factor receipts formula to determine the percentage of the nonresident taxpayer's income that is taxable. The single-factor receipts formula is derived by dividing the gross receipts attributable to transacting business in Indiana by the taxpayer's total receipts from transacting business in all taxing jurisdictions.

TAX RATE

The tax rate for the FIT is 8.5 percent for taxable years beginning before Jan. 1, 2014. However, the rate decreases in the following manner for the following time periods:

- For taxable years beginning after Dec. 31, 2013, and before Jan. 1, 2015, the rate is 8.0 percent.
- For taxable years beginning after Dec. 31, 2014, and before Jan. 1, 2016, the rate is 7.5 percent.
- For taxable years beginning after Dec. 31, 2015, and before Jan. 1, 2017, the rate is 7.0 percent.
- For taxable years beginning after Dec. 31, 2016, the rate is 6.5 percent.

EXEMPTIONS AND EXCLUSIONS

Four specific types of corporations are exempted from the financial institutions tax:

- Insurance companies subject to the tax under [IC 27-1-18-2](#) or [IC 6-3](#);
- International banking facilities (as defined in Regulation D of the Board of Governors of the Federal Reserve System);
- Any corporation that is exempt from income tax under Section 1363 of the Internal Revenue Code; and
- Nonprofit corporations.

An exclusion is also provided for those financial institutions whose Indiana activities are limited to certain activities. These activities include owning an interest in the following types of property, including those activities within Indiana that are reasonably required to evaluate and complete the acquisition or disposition of the property, the servicing of the property or the income from the property, the collection of income from the property, or the acquisition or liquidation of collateral relating to the property:

- An interest in a real estate mortgage investment conduit, a real estate investment trust, or a regulated investment company (as those terms are defined in the Internal Revenue Code);
- An interest in a loan-backed security representing ownership or participation in a pool of promissory notes or certificates of interest that provide for payments in relation to payments or reasonable projections of payments on the notes or certificates;
- An interest in a loan or other asset in which the interest is attributed in [IC 6-5.5-4-4](#), [IC 6-5.5-4-5](#), and [IC 6-5.5-4-6](#) and in which the payment obligations were solicited and entered into by a person who is independent and not acting on behalf of the owner;
- An interest in the right to service or collect income from a loan or other asset from which interest on the loan or other asset is attributed in [IC 6-5.5-4-4](#), [IC 6-5.5-4-5](#), and [IC 6-5.5-4-6](#) and in which the payment obligations were solicited and entered into by a person who is independent and not acting on behalf of the owner; and
- An amount held in an escrow or a trust account with respect to property described in this subdivision.

COMBINED RETURNS

A taxpayer is allowed to file a separate return only in those instances where the taxpayer is not a member of a unitary group. If the taxpayer is a member of a unitary group, combined reporting is mandatory. However, if the taxpayer determines that its Indiana income is not accurately reflected by the filing of a combined return, then the taxpayer may petition the department by indicating on its annual return that the return is a separate return made by a member of a unitary group. Such petition is subject to approval by the department.

If a combined return is warranted, each taxpayer that is a member of a unitary group is obligated to file as a part of the combined return that includes all operations of the unitary business, but the unitary group should collectively file one return. The statute requires that the combined return include the adjusted gross income of all members of the group that are transacting business wholly or partially within Indiana. The statute provides an exclusion for the income of corporations or other entities organized in foreign countries, except a federal or state branch of a foreign bank or its subsidiary that transacts business in Indiana. In other words, combined reporting is

on a "water's edge" basis.

"Unitary business" means business activities or operations that are of mutual benefit, dependent upon or contributory to one another, individually or as a group, in transacting the business of a financial institution. The term can be applied within a single entity or between multiple entities and without regard to whether each entity is a corporation, partnership, or trust.

"Unitary group" means those entities that are engaged in a unitary business wholly or partially within Indiana. Unity is presumed if there is unity of ownership, operation, or use as evidenced by centralized management, centralized purchasing, advertising, accounting, or other controlled interaction among entities that are members of the unitary group as defined in [IC 6-5.5-1-18\(a\)](#). In other words, members of a unitary group are limited to those members who meet the definition of "taxpayer" for purposes of [IC 6-5.5](#).

Unity of ownership exists for a corporation if it is a member of a group of two or more business entities, 50 percent of whose voting stock is owned by a common owner or owners or by one or more of the member corporations of the group.

COMPUTATION

Taxpayers, with the exception of credit unions and investment companies, compute the FIT as follows:

Federal Taxable Income (IRC Section 63)

A. Add the amount of deductions/losses included in federal income tax return not allowed on the Indiana return:

- (1) Net operating losses (NOL)
- (2) Net capital losses
- (3) Bad debt deductions
- (4) Charitable contributions
- (5) State and local income and franchise taxes
- (6) Bonus depreciation under Section 168(k) of the Internal Revenue Code (IRC)
- (7) Section 179 of the IRC concerning business expense deductions that exceed \$25,000
- (8) Domestic production activities deduction under Section 199 of the IRC
- (9) Add or subtract the amount necessary to make the adjusted gross income of any taxpayer that claimed the special allowance for qualified disaster assistance property under Section 168(n) of the IRC
- (10) Add or subtract the amount of qualified refinery property that was expensed under Section 179 of the IRC
- (11) Add or subtract the amount of qualified expenses for a qualified film or television production under Section 181 of the IRC
- (12) Add or subtract the amount necessary to make the adjusted gross income of any taxpayer that treated a loss from the sale or exchange of preferred stock in:
 - (i) the Federal National Mortgage Association; or
 - (ii) the Federal Home Loan Mortgage Corporation;
 as an ordinary loss under Section 301 of the Emergency Economic Stabilization Act of 2008 in the current taxable year or an earlier taxable year equal to the amount of adjusted gross income that would have been computed had the loss not been treated as an ordinary loss
- (13) An amount equal to any exempt insurance income under Section 953(e) of the IRC

B. Interest income on state and municipal obligations not

	included in federal taxable income	
DEDUCT:	A. Bad debts actually charged off	(_____)
	B. Associated expenses to carry state and municipal obligations (I.R.C. Section 265)	(_____)
	C. Bad debt reserve transition adjustment included in federal taxable income because of a tax accounting method change	(_____)
	<u>Indiana Adjusted Gross Income</u>	=====
	Apportionment factor:	
	<u>Receipts attributable to Indiana</u>	
	Total receipts	= _____%
	Indiana Apportioned Income	_____
DEDUCT:		
	* Indiana net operating losses (NOL)	(_____)
	**Indiana net capital losses (deductible to the extent of net capital gains)	(_____)
	Indiana Taxable Income	_____
	Multiplied by the Appropriate Tax Rate Tax before Credits	_____
	*** Less: Nonresident taxpayers Credit	(_____)
	Indiana Financial Institutions Tax Liability	=====

*Indiana's net operating loss (NOL) for the nonresident taxpayer is multiplied by the apportionment factor. If there is negative taxable income when the FIT income is determined, the same may be carried forward. Such carryforward may be carried forward 15 years. Losses are not carried back.

**A taxpayer's Indiana net capital loss for the taxable year equals the taxpayer's net capital losses for the taxable year minus the net capital gains for the year multiplied by the apportionment percentage applicable to the taxpayer under [IC 6-5.5-2](#) for the taxable year of the loss. A net capital loss for a taxable year may be carried forward to each of the 5 succeeding taxable years.

***A nonresident taxpayer is entitled to a credit against the tax due under this article for the amount of net income tax due to the nonresident taxpayer's domiciliary state for a taxable year if:

- The receipt of interest or other income from a loan or loan transaction is attributable both to the taxpayer's domiciliary state under that state's laws and also to Indiana under [IC 6-5.5-4](#); and
- The principal amount of the loan is at least \$2,000,000.

The amount of the credit for each taxable year is the lesser of:

- The portion of the net income tax actually paid by the nonresident taxpayer to its domiciliary state that is attributable to the loan or loan transaction; or
- The portion of the FIT due to Indiana under this article that is attributable to a loan or loan transaction. The amount of tax attributable to a loan or loan transaction is the portion of the total tax due to each state in an amount equal to the same proportion as the receipts from the loan or loan transaction bear to the taxpayer's total receipts.

In the case of a nonresident credit union, "adjusted gross income" for a taxable year means the total transfers to undivided earnings minus dividends for that taxable year after statutory reserves are set aside under IC28-7-1-24, multiplied by their apportionment factor.

In the case of a nonresident investment company, "adjusted gross income" means the company's federal taxable income, plus the amount excluded from federal gross income under Section 103 of the Internal Revenue Code for interest received on an obligation of a state other than Indiana, or a political subdivision of such a state, that was acquired by the taxpayer after Dec. 31, 2011, multiplied by the quotient created by:

- The aggregate of the gross payments collected by the company during the taxable year from old and new business upon investment contracts issued by the company and held by a resident of Indiana; divided by
- The total amount of gross payments collected during the taxable year by the company from the business upon investment contracts issued by the company and held by persons residing within Indiana and elsewhere.

PAYMENT OF THE TAX

The FIT is payable directly to the department. Quarterly estimated payments are required if the taxpayer's annual

liability exceeds \$2,500. If the taxpayer's quarterly estimated payments exceed \$5,000, the estimated payment must be made by electronic funds transfer.

Michael J. Alley
Commissioner

Posted: 11/27/2013 by Legislative Services Agency
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